

STATEMENT BY
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BEFORE THE
HOUSE GOVERNMENT REFORM COMMITTEE,
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INTERNATIONAL RELATIONS

“THE DEVELOPMENT FUND FOR IRAQ”

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Introduction

Good morning. I am COL Emmett Du Bose. I currently serve as the Deputy Commander of the Southwestern Division, U.S. Army Corps of Engineers (USACE), in Dallas, Texas. Prior to this assignment, I was stationed in Iraq from October 2003 through June 2004 and served as the Second Task Force Commander and Director of the "Restore Iraqi Oil" or RIO Program. My primary assigned mission was to work cooperatively with the Iraqi people to safely and effectively restore the oil infrastructure of Iraq to enable the economic recovery of Iraq.

Funding for this effort involved both US and Iraqi sources, to include the Development Fund for Iraq, or DFI. DFI-funds were used for both infrastructure restoration services and the importation of refined fuels under the original Corps RIO contract. I have been asked to review with you today the status of DCAA audit reports on the DFI-funded task orders for that contract.

Overview of KBRS-RIO Contract

The RIO contract, which was physically completed last year, is a cost reimbursement contract consisting of 10 task orders (T.O.s). Two U.S.-funded T.O.s are also fiscally complete (1 and 2) and another U.S.-funded T.O. is fiscally complete, pending claim resolution (4). The remaining seven T.O.s, to include the six DFI-funded T.O.s, are still in the definitization process (3 and 5-10).

Since this is a cost-plus award fee contract, it requires Defense Contract Audit Agency (DCAA) audits as an integral part of the contract definitization process in which we are now engaged. At the request of the Contracting officer, DCAA has completed 20 audit reports, and is actively working on several others, in support of this effort. Fifteen of these audit reports have been in support of DFI-funded task orders. The Contracting Officer is using the information provided by DCAA, along with information from USACE

field representatives and advisors to complete remaining negotiations and make award fee determinations.

Task Orders (T.O.) #5, 7, 8, 9 and 10

Five of the six DFI-funded T.O.s were issued to meet emergency humanitarian fuel requirements by importing refined petroleum products. It became clear to USACE that we would be assigned the task of importing and distributing humanitarian fuel products on 17 April 2003. At that time, there were serious shortages of refined petroleum products. Gasoline lines stretched for long distances in Baghdad. To keep order in these lines, soldiers had to leave their armored vehicles. One soldier recently had been killed attempting to keep order. There was high level concern about the volatile situation the shortages were creating.

Task Force RIO believed that any humanitarian fuel mission should be given to USAID. Alternatively, Defense Energy Support Command (DESC), LOGCAP contract or Combined Forces Land Component Command of Central Command (CFLCC) Logistics already were used to provide similar logistics functions for the military. All seemed better suited to fulfill this requirement than the Task Force RIO, which, despite the broad scope of the original RIO contract was principally established to provide engineering services for oil infrastructure restoration. We understand DESC, LOGCAP and CFLCC Logistics also took the position that the import and distribution of humanitarian fuels were not part of their mission.

Task Force RIO was concerned that executing this fuel importation mission would detract from its ability to focus on the repair and restoration of the petroleum infrastructure (which it did), and that the use of funds allocated for this purpose would divert the funding necessary for oil infrastructure restoration.

On or about 4 May 2003, CFLCC issued an order tasking RIO to execute this mission. Discussions regarding statutory and contractual authorities for use of the RIO contract

to perform the mission and how it could be funded followed. Eventually, all concluded that the requisite authority was available and the Coalition Provisional Authority (CPA) determined that DFI funds would be used for the mission. On 4 May 2003, CFLCC officially assigned Task Force RIO the first humanitarian fuel mission. The contracting officer immediately issued a task order to KBRS requiring the import and distribution of humanitarian fuels. Once assigned this mission, the RIO team did its best to execute the mission successfully.

Task Force RIO received funding for this contract in increments as it became available. There were 15 changes in funding in the first three months of the mission alone. Over the life of the mission, RIO received more than 30 days of funding only 4 times (31, 36, 41, and 68 days). On three occasions, RIO received only 2 days of funding. On four of the occasions when larger amounts of funds were received, some of those funds were later revoked. Consequently the costs of executing this fuel mission were higher than they would have been if USACE had been provided sufficient funds to direct the contractor to enter into longer term purchases of fuel.

In December 2003, the DESC was directed by DoD to begin planning efforts to assume the humanitarian fuel mission. This mission was formally transferred to DESC on 1 April 2004. DESC, unlike RIO, had several months to plan its procurement. In addition, it received sufficient funds up front to contract for 90 days for fuel purchases and deliveries. These were significant factors in the different pricing DESC was able to achieve when it assumed responsibility for the mission.

The urgency, magnitude, complexity and hazardous conditions under which the RIO task orders were performed is unprecedented. These were contributing factors which, along with KBRS estimating system challenges, led to the multiple revisions of KBR proposals and resulting multiple revisions of DCAA audit reports. All together, there have been 14 DCAA audit reports on these fuel T.O.s, nine of which have been superseded. The DCAA audit reports, to include all questioned costs, are being used by the contracting officer, in conjunction with the Government's contract performance

information and the contractor's proposals, to establish the Government's position, from which the contracting officer will negotiate final payment on the various task orders and determine the award fee. We are currently in the middle of this process and intend to finalize the effort before the end of summer. In the meantime, the Government is currently withholding payments of approximately \$68 million, plus all possible award fees, pending settlement of these T.O. payments.

T.O. #6

The other DFI-funded T.O. is #6. It involved the design and construction of multiple pipeline crossings of the Tigris River at Al Fatah, near Bayji, as well as multiple power generation stations required to support the operation of oil production, distribution and refineries across Iraq. It also required KBR to provide equipment, supplies and technical services to support the Iraqi Oil Ministry's efforts to build a 40-inch diameter pipeline from Kirkuk to Bayji.

DCAA has already completed one audit report on this effort and is now working on what we believe will be the final T.O. 6 audit report. We expect the final audit report to be completed by July, after which the contracting officer will definitize the task order and negotiate final payment with the contractor.

Use of DCAA Audit Reports

The audit process on this cost contract has been iterative. When the contractor submits a revised proposal, the revision is audited by DCAA. As part of this process, the contractor, contracting officer and other advisors provide frequent updates and additional information that often leads to modifications of the original draft audit report. For example, an early DCAA audit report of a KBRS fuel T.O. identified a \$27 million of costs for the transportation of liquid petroleum gas, or LPG. Based on a comparison of transportation costs and the quantity of LPG on a specific task order, the transportation costs appeared to be unreasonable, given the small amount of LPG product shown on the task order. When the audit report was reviewed by KBRS, they found that the bulk

of LPG product that had been transported was actually accounted for under a different task order. As a result, the \$27 million in questioned cost was resolved.

DCAA Questioned Costs

In a cost contract of this magnitude and complexity we expect there to be questioned or unsupported costs in audit reports. So it is not surprising that DCAA questioned certain costs of DFI-funded T.O.s. In its final audit reports, we expect that DCAA will continue to question certain costs on the DFI-funded T.O.s. Moreover, it is important to understand that DCAA does not question whether KBRS actually incurred any of these costs; instead, DCAA questions primarily whether KBRS might have been able to obtain some services at a lower cost than they acquired them. Some of the questioned costs addressed in previous audit reports have now been resolved, resulting from changes in the KBRS proposals or by additional information provided by KBRS. As usual in large cost contracts, we expect some cost issues will remain, even after the adjustments DCAA has made to its final audit reports. Also, as usual, the contracting officer is responsible for resolving those issues.

In making his decisions, the contracting officer carefully weighs the advice provided by DCAA, contracting personnel and other advisors appropriate for the circumstances, such as DCMA. The contracting officer fully considers the advice of DCAA, just as he considers the advice of these other advisors. The final decision on the weight to be given to any advice depends on the contracting officer's evaluation of that advice.

Redacted KBRS Audit Reports

USACE officials received a request to provide audit reports of sole-source DFI-funded contracts to the International Advisory and Monitoring Board (IAMB). The Office of Chief Counsel was consulted due to concerns about the release of proprietary data outside official U.S. government channels. When Office of Chief Counsel advised that USACE could not release confidential commercial information to sources outside the

U.S. government without contractor consent, USACE officials asked KBRS if they would agree to releasing the audit reports to the IAMB. KBRS informed USACE that they would not agree to provide the audit reports, asserting that the audits contained their proprietary information and that the government was prohibited from releasing that information under the Trade Secrets Act. USACE Office of Chief Counsel advised that unredacted audits could not be released to the IAMB without contractor consent. The USACE Office of Chief Counsel coordinated with the DoD Office of General Counsel in providing this advice.

Recognizing that we could not provide the IAMB unredacted audit reports, we sought a method to provide as much information to the IAMB as possible. Accordingly, we requested that KBRS review the DFI-funded T.O. audit reports and redact information they believed was protected under the Trade Secrets Act. KBRS provided USACE with redacted audit reports and a letter authorizing USACE to release the redacted audit reports to the IAMB. Counsel noted that there were significant legal risks, to include potential individual criminal violations, associated with changing the redactions provided by KBRS.

USACE and DoD personnel delivered the redacted copies of the KBRS DFI audit reports on five of the six task orders to the IAMB in New York in October 2004. The audit report of the sixth task order was not complete at that time, but was delivered soon thereafter. No requests to provide additional information to the IAMB have been tasked to USACE since that time.

Summary

Six Task Orders on the RIO contract were funded with DFI funds. Five involved fuel import and distribution. There have been a total of 14 audit reports and additional advice from DCAA on these task orders. One involved repairs to the Iraqi oil infrastructure. There has been one audit reports with one additional audit report pending on this task order.

Some costs that have been questioned or found to be unsupported in previous audit reports have been resolved, either by changes in the KBRS proposals or by additional information provided to the auditors. We fully expect that, although there is no question concerning whether or not KBRS actually incurred these costs, DCAA audit reports will continue to question KBRS business judgment in incurring some of these costs. These questions will be resolved by the contracting officer in the near future, based on input from DCAA, DCMA and other advisors as appropriate. The job now is to use the information at our disposal to assist the contracting officer in reaching a fair and equitable settlement of these task orders with the contractor, while fully protecting the public interest.